UNIVERSITY OF TORONTO | SCHOOL OF CITIES | Highline Beta

SUMMARY BRIEF

HOUSING FINANCE FORUM: ADUs, MULTIPLEXES, AND OFF-SITE CONSTRUCTION

September 2024

Hosted by:

School of Cities and Highline Beta

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DESIGN

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TABLE OF CONTENTS

EXECUTIVE SUMMARY

The availability of financial products for accessory dwelling units (ADUs), multiplexes, and off-site modular construction is a key enabler for scaling these types of housing. Although demand for these housing solutions is growing, the development of financial products is lagging behind housing innovations, creating a bottleneck for scaling and producing more housing units. To address this, the School of Cities and Highline Beta—scaling hubs for the Housing Supply Challenge's *Level Up* initiative—organized the Housing Finance Forum on September 27th to address the financing concerns. The forum aimed to bring stakeholders together to discuss financing needs and solutions for ADUs, multiplexes, and off-site modular construction. Forum attendees included representatives from participating innovators Resimate, ReHousing, Mddl, Vancity, UTILE, BuildingIN, and related stakeholders including RBC, BMO, Desjardins, National Bank, Canada Guaranty, CMHC, The Circle Community Land Trust, Foundry Mortgage Capital, Pomegranate Housing Consultancy, Peoples Group, and Meridian Credit Union.

This report summarizes the participant discussions from three simultaneous workshops held during the forum:

FINANCING ADUS

Participants discussed the challenges that homeowners face in understanding the amount they can borrow, and in securing appropriate financing for renovation or construction projects such as ADUs and multiplex conversion. A key suggestion was the creation of a one-stop online platform offering personalized financing options, educational resources, and expert advice. The session highlighted the need for standardized information, clearer distinctions between owners and developers, and a focus on affordability. Participants proposed new financial and insurance products, along with policy changes to support ADU financing. Key recommendations and takeaways included mapping the end user financing journey, aggregating current resources, adjusting policies, and piloting flexible alternative financing models. Importantly, continued collaboration and engagement among stakeholders were emphasized to advance these initiatives.

FINANCING MULTIPLEXES

Participants discussed the challenge faced by small-scale developers to access sub-$5 million loans in order to build middle housing developments. The discussion highlighted key ideas and solutions, categorized into education, financing, lending, and implementation strategies. Participants emphasized the need to educate homeowners and small-scale developers on financing risks, and to advocate for new lending practices that support middle housing. Specific financing programs were proposed, such as a first-time investor program and middle financing solutions for small-scale developers. Additional suggestions included tax incentives for property upgrades, partnerships between nonprofits and developers, and collaborative financing models. Key takeaways emphasized transparency in risk assessment and designing financial products tailored for diverse developers' needs. Recommendations and takeaways focused on closing the financing gap, assessing risk profiles, and fostering collaboration among stakeholders.

FINANCING VOLUMETRIC MODULAR HOUSING (MARKET AND NON-MARKET SECTORS)

The main challenge for non-market housing discussed by participants was accessing conventional financing, due to high deposit requirements that are not covered by CMHC or traditional financiers. As a result, non-market developers have to rely on costly non-conventional lenders, which increases project costs and limits scalability. The cashflow requirements of modular construction further complicate financing. Participants also discussed challenges for market housing, where the absence of modular construction-specific products and hesitance of lenders to finance these projects due to the perceived risks, are constant barriers. Misconceptions about modular construction, like doubts about its permanence, hinder access to financial products. These barriers prevent small-scale developers from scaling modular market housing projects efficiently.

Participants identified potential solutions, including the need for CMHC to support deposit payments for affordable housing and a government-backed loan guarantee program to mitigate lender risks. Developing a pre-approved list of modular manufacturers and exploring pilot programs with flexible financiers (such as Vancity) were also proposed to encourage financing for both market and non-market housing.

INTRODUCTION

Our conversations with some of the participant innovators revealed that the clients for accessory dwelling units (ADUs), multiplexes, and off-site construction have special financing and timeframe needs that do not fit the financial models available on the market. These financing gaps pose a significant and continuous barrier to uptake of housing solutions by clients, and are hindering the scaling of the Housing Supply Challenge (HSC) solutions.

The Housing Finance Forum (HFF) was organised to encourage circular discussions and collaborative problem solving by bringing together innovators, financiers and concerned stakeholders. The forum took place on September 27th, 2024, and featured thematic workshops in three streams: ADUs, multiplexes, and off-site construction. Each stream dealt with financing challenges associated with that building type or construction method. The workshops were designed to be solutions-oriented and to promote collaboration and knowledge exchange in small group settings of 8-12 people.

> *The HFF was organised to encourage circular discussions and collaborative* ***problem solving by bringing together innovators, financiers and concerned stakeholders.***

Three one-hour sessions were designed and facilitated concurrently following the framework:

Session 1: Problem statement deep
Session 2: Solution brainstorm
Session 3: Key takeaways and actions

Prior to the breakout workshop sessions, the participating HSC innovators presented their innovative housing solutions, and the main financial barriers standing in their way. The presentations and the full list of attendees can be found here.

The outcome of the forum was two-fold:

1. Summarize the key challenges, potential solutions, and next steps to creating an actionable roadmap to improving access to finance
2. Cultivate relationships between innovators and key players that will accelerate collaboration and partnerships and initiate new approaches and solutions

ACCESSORY DWELLING UNITS (ADUs)

Facilitated by Veronika Kvon, Highline Beta, Program Director

HSC innovators

ReHousing is a non-profit focusing on housing creation through applied research, consultation and education. ReHousing bridges the gap between emerging policy initiatives and the housing creators they intend to serve. Their website is designed to empower citizen developers in converting single-family homes into multi-unit housing.

1. Co-Founder, Michael Piper represented ReHousing

Resimate offers turnkey services to help homeowners navigate the backyard home building process from design to installation. They streamline the modular construction process for ADUs through a centralized online marketplace. The marketplace brings together ADU manufacturers and development support to offer homeowners a turnkey solution that makes building ADUs quicker and easier.

2. Co-Founder & CEO, Sarah Cipkar represented Resimate

Participants

	Name	Organization	Title
3.	Tracie Cheung	RBC	Home Equity Financing
4.	Lesli Gaynor	GoCo Solutions	Chief Executive Officer
5.	Gracen Johnson	CMHC	Senior Specialist, Innovation and Research
6.	Lara Muldoon	School of Cities	Assistant Director, Strategic Partnerships and Initiatives
7.	Matt Pickering	National Bank of Canada	Mortgage Development Manager
8.	Mirela Pirlea	Desjardins	Lead Partnerships Innovation and Entrepreneurship Ecosystems
9.	Geoff Scott	Canada Guaranty	Senior Vice President, Operations

SESSION 1: PROBLEM STATEMENT DEEP DIVE

Prior to the session, the innovators were asked to share their views on the top challenges faced by their adopters related to securing financing for their housing solutions. The innovators' responses were collated into the following problem statement to serve as the initial kick-off point for the round table discussions:

"For Canadian homeowners with existing mortgages, it is challenging to understand the amount they can borrow and secure financing for renovation/construction projects such as accessory/additional dwelling units (ADUs) and multiplex conversion."

The group engaged in a fruitful discussion with the end goal of gaining a deeper understanding of the problem, its attributes, existing solutions, and potential gaps. All the participants shared their unique perspectives, raised probing questions, and shared innovative practices and approaches that are employed by their organizations or in the industry. As a result, the following themes emerged:

Citizen developers vs for-profit developers

The discussion led to the agreement that it is important to differentiate the intended use of the development: is it for family use, or is it to generate financial returns? There are multiple ways that resources can be pooled, and the starting point should be the intended purpose. This will determine the risk profile and set the direction for available financing options that include traditional lenders, specialized products, government supports, or alternative models such as co-ownership.

One of the ways some financiers mitigate risk is by evaluating the future property value and cash-flow based on future rents from additional units. From lenders' perspective, it is easier to finance a home with rental income and obtain a market-rent appraisal. It was suggested that financing based on rental appraisals can incentivize building units for rental purposes, rather than housing people. On the other hand, a point was brought up that market-rent appraisals might help increase supply and eventually drive the costs down. There is not enough data currently available to understand the split between the two camps, and the group agreed it is an important statistic that needs to be tracked and evaluated in the future. The appraisal process is a critical step and should be embedded in the solution.

Current solutions landscape and limitations

Currently, there are solutions and interest from public and private sectors to support gentle density projects like ADUs and multiplex conversions. Some recent announcements include specialized products like RBC Construction Mortgage for Multi-Units Program, Laneway House Mortgage by Equitable Bank, and a government proposal for the Secondary Suite Loan Program.

Some players, like National Bank and Desjardins, offer services by adapting existing products and tools to customers' specific needs, but there are limitations associated with this approach. For example, the financing for additional units involves taking over the whole mortgage, which limits the options for borrowers and creates a timing issue.

At Desjardins, each mortgage comes with a line of credit backing the house, allowing homeowners to access pre-approved funds as needed. Although this is not a common practice, it is one of the examples where traditional players alleviate the barriers to financing additional units.

The use of purchase plus loans for building an ADU was brought up as a potential avenue. Although there were some instances noted by NBC where lenders are willing to allow purchase-plus for ADUs, the borrower needs to have a permit in place before any money is advanced and must comply with all the zoning regulations.

Some financiers are better positioned to service the emerging market, but many lenders are hesitant to get involved in these complexities because they don’t want to deal with financing for builders, especially if they don’t have the necessary in-house expertise.

Lack of education and awareness among homeowners

It was also discussed that early adopters - who are more sophisticated and experienced developers - tend to find a way to pool the resources and finance the project, but there is a huge lack of broader awareness among the first timers. It was agreed that communication about financing tools, methods, and options is the top priority. Not enough consumers know how to approach a project or assess their options. There are resources and tools currently available - such as AI-powered chatbots, specialized expert supports, how-to-guides, and ADU calculators - but the information tends to be limited, fragmented, applicable to a narrow niche of adopters, or not easily accessible online.

> ***Standardized practices and language among lenders and municipalities are important*** *for fast-tracking the adoption and lending processes.*

Need for standardization and streamlined pre-approval process

Standardized practices and language among lenders and municipalities are important for fast-tracking the adoption and lending processes. Edmonton, for example, has standardized its categories: two-unit, three-unit, four-unit, etc. and some municipalities can say no to an ADU where there is already an existing duplex. Simplifying and standardizing these categories is important to providing scalable solutions.

Early-stage approvals with municipalities were also discussed as a potential solution to expediting the lending process, but at this stage municipalities are hesitant, based on innovators' experience.

SESSION 2: SOLUTIONS BRAINSTORM

The goal for Session 2 was to generate as many ideas for potential solutions as possible that can tackle the problem and its critical attributes. The following "How might we..." statement prompts were generated by the group to kick off the brainstorming session:

- *How might we help homeowners understand the amount they need?*
- *How might we find ways to enhance or launch new financial & insurance products?*
- *How might we improve qualification for homeowners developing additional unit?*
- *How might we expand units nationally while keeping housing affordable?*
- *How might we build awareness among homeowners about available options?*

Each member generated ideas for potential solutions. The group was encouraged to generate as many ideas as possible, regardless of feasibility or time horizon. Everyone presented and discussed their list in a group, and the ideas were grouped into the following themes.

One-stop-shop online navigator/aggregator resource

- A questionnaire to determine the various financing needs with potential options, current offerings, referrals to lenders, and alternative ownership models. This could help in creating tailored, customized, "choose your own adventure" financing options.
- Educational directory with case studies, video explainers, and success stories.
- A standardized quick assessment & forecasting tool based on category, project, purpose.
- A universal financing checklist that is public, transparent and open for prequalification.
- Access to expert advice i.e., chatbot or a person that can help answer both financing and site feasibility questions to help homeowners prepare for their financing application.

New financial and insurance products

- Insurance (Mortgage Loan Insurance Select potentially) available for multi-property ADU conversions (2-5 units spread out on multiple sites)
- New fractional mortgage product by fintech companies to facilitate co-ownership
- New specialized products from traditional financing players with clear guidelines and expert support

New policy

- Expand municipal pre-approval process to better suit new unit financing
- New federal financial policy specific to detached ADUs

SESSION 3: KEY TAKEAWAYS AND ACTIONS

The final hour was dedicated to individual and group reflections, where everyone shared their personal takeaways and learnings. One of the most common takeaways from each participant was to further investigate the available solutions, gaps and ideas discussed during the day. Some follow-up engagements were established between participants to explore collaboration and referral partnerships. Overall, the group agreed that a collaborative approach and continued conversation with concerned stakeholders is required to move the proposed initiatives forward.

Below is the consolidated list of key takeaways and the call to action from the group.

Takeaways

- Homebuyers who want to add additional units face educational and structural barriers.
- There is a huge need to consolidate and standardize information online.
- The distinction between owner and developer is important
- There is a need to talk more about affordability, not just a means for additional income
- There is a need for data collection and a study to analyze the split between ADUs developed as rental units, and those developed for other uses
- There are multiple entry points to this journey and multiple ways that resources can be pooled
- The private sector is eager to grow into this space
- There are flexible options available, but they're relatively new or tend to be under the radar because they're driven by an individual or a small team
- Municipal pre-approval and federal government policy can help lower financing barriers and accelerate adoption
- Language use is important and standardized guidelines for lenders and borrowers are needed for faster adoption

Recommended actions

- Map out financing journey from different end-users' perspectives
- Aggregate current solution providers, tools, and case studies and make them publicly available
- Investigate if current policies or offerings can be adjusted or better positioned to service customers' needs
- Develop nationwide lending and insurance guidelines to support refinancing for additional units
- Build awareness among end users and provide them with accessible expertise to help them navigate the regulatory, financing, and construction processes
- Assess, explore, and pilot new flexible financing products by leveraging new financing models and fintech technologies
- Follow up engagement between participants to explore collaboration and referral partnerships

MULTIPLEXES

Facilitated by Ben Yoskovitz, Highline Beta, Founding Partner

HSC innovators

ReHousing is a non-profit focusing on housing creation through applied research, consultation and education. ReHousing bridges the gap between emerging policy initiatives and the housing creators they intend to serve. Their website is designed to empower citizen developers in converting single-family homes into multi-unit housing.

1. Executive Director, Samantha Eby represented ReHousing

MDDL is a non-profit organization that builds capacity for the delivery of middle housing in Canada. It offers education, support, and advocacy for developers, and homeowners. Their mission, alongside strategic partners, is to build capacity from top to bottom, and to strategically partner with municipalities, industry experts and citizens in reducing barriers and delivering middle. MDDL provides the tools and resources to successfully embrace middle housing development.

2. President, Darlene Jehn represented MDDL

Participants

	Name	**Organization**	**Title**
3.	Alia Abaya	The Circle Community LandTrust	Chief Executive Officer
4.	Dinesh Achria	Foundry Mortgage Capital	Commercial Mortgage Agent
5.	Mihai Aldea	RBC	Director, Home Equity Financing, Builder program
6.	Swamy Krishnamoorthy	BMO	Group Product Manager, Home Financing
7.	Danielle Millett	CMHC	Specialist, Innovation

SESSION 1: PROBLEM STATEMENT DEEP DIVE

Through a pre-workshop survey, we gathered initial thoughts from the innovators on the financing challenges they and/or their clients face in multiplex development. Their responses were combined into the following problem statement to serve as the initial kick-off point for the round table discussion:

"For small-scale developers, it is challenging to access sub-$5 million loans in order to build middle housing developments. With limited financing options, projects experience delays and higher costs due to increased land holding, with some projects entirely failing to advance."

This session was further primed by the innovator presentations on their products and the challenges they face in scaling their housing solutions. ReHousing spoke to the misalignment of funding and policy initiatives that leverage the citizen developer's equity in a predatory way. MDDL spoke about challenges in accessing sub- $5 million loans for new developers. They also brought up other challenges, including compliance or slide-offs in covenant funds, and land financing.

The group engaged in a nuanced discussion with an end goal to gain a deeper understanding of the problem, root causes, existing solutions, and potential gaps. All the participants shared their unique perspectives, raised clarifying questions, and shared innovative products and approaches. As a result, the following themes emerged:

Difference between owner occupied and investor developments

The homeowner developer[1], developer for family[2], and investor-developer[3] must be recognized as different personas in the playing field. Commercial banks often see multiplex development on single-family lots as a strategy to leverage existing land to earn additional profit through rental income. These practices can result in distortions in the rental market. Therefore, commercial banks often have mechanisms in place to avoid BRRR (buy refinance rebuilt rent) investors.

The participants discussed if the term "investor" has a branding issue, with a negative stigma attached of personal monetary gain. Given the current scope to increase overall density, and the need for additional units on the market, the profit margins of individuals should perhaps not be considered as a deterrent.

Middle financing

The innovators observed that if small developers are successful in their first project, they typically develop more, which effectively means more players and units. Small business developers are a market of their own and, in some ways, have a foot both in commercial and personal finance.

The participants discussed how most personal financing options have a cap of $2 million while commercial financing portfolios start at $5 million, and that missing middle developments of 6-8 units typically cost between $2-5 million. It was recognized that the market is generally missing the 'middle financing' space.

Middle housing in bigger markets

The participants discussed the suitability of Mortgage Loan Insurance Select (MLI Select) for bigger markets while recognizing its place for prioritizing affordability along with supply. MLI Select offers incentives such as lower interest rates for new construction and existing properties. Though, the program appears to come with a clause for properties that are demolished requiring the applicant to cover the loss of value of the asset on top of construction, limiting the incentive for demolition projects. The program also comes with an affordability criterion that is often difficult to meet in bigger markets like Toronto and Vancouver.

Within the MDDL ecosystem, covenant fund is offered to known developers and does not have minimum net worth requirements. It covers an envelope of expected cost overruns in the project. The fund relies on a list of pre-approved builders who can provide guarantees on the project costs upfront. Here, compliance and slide offs are important aspects to consider and monitor.

Inclusionary zoning, where applicable, requires adding affordable units alongside market unit development in certain residential zones. A caveat to note is that it may further the divide between market unit zones and affordable housing zones in the city. There is precedence for market and affordable housing development in the same building, if the project is stratified. However, malicious practices may enable the developer to default, resulting in the removal of the affordability requirement.

> *Commercial banks often offer* ***special programs, under the same mortgage channels, for certain occupations*** *that are less susceptible to a downturn.*

Risk assessment

There are many professional and unprofessional developers in the market which may not fit the traditional boxes and are deemed risky without being given a fair opportunity. Commercial banks often offer special programs, under the same mortgage channels, for certain occupations that are less susceptible to a downturn. They are considered less risky borrowers and easier to work with according to the Four Cs of Credit.[4] These occupations include doctors, lawyers, and dentists, amongst others.

In June 2024, RBC launched the Construction Mortgage Multi-Units Program to assist with owner-occupied developments of up to six housing units. Under the program, RBC considers adding the projected market rent earnings from the unit(s) as eligible supplementary income, which in turn can help support obtaining a mortgage. However, there may be a higher interest rate for a development above four units. The program does not have net-worth minimums, but requires 10-20% liquidity (in the form of cash or easily convertible to cash). In addition, to mitigate segmentation risk, the bank analyzes the builder's credit bureau history, experience, CHBA membership status and social media reviews.

Inconsistent policies

Three levels of government without a central body that manages housing leaves market players in a difficult situation. There is a lot of confusion and a lack of clarity due to the variables at play across the country.

SESSION 2: SOLUTIONS BRAINSTORM

The goal for this session was to generate ideas for potential solutions to the problem and its critical attributes. The group was encouraged to generate as many ideas as possible, regardless of feasibility or time horizon. The following "How might we..." statement prompts were generated by the group to kick off the brainstorming session:

How might we differentiate between owner occupied and developments?
How might we help people who fall between personal and commercial financing?
How might we make financially viable lending mechanisms for middle housing in bigger markets?
How might we underwrite deals at the ward level?
How might we achieve policy uniformity and consistency across the country?

The participants' ideas and solutions were grouped into the following categories:

Education and awareness

- Educate and empower homeowners and small developers about middle housing development to get more units into the market.
- Offer transparency in risk calculation so that citizen developers are prepared to speak to lenders.
- Challenge the status quo of lending practices that deem the owner-occupied development to be less risky than an investor home.
- Conduct a thorough risk assessment with current data to allow for a new balance between the lenders risk and motivations of the different developers without overleveraging personal equity. Involved stakeholders need to conduct a gap assessment to understand the associated risks in financing all these projects.

Middle financing

- Design specific programs to suit the needs of small businesses – developments in the range of $2 million and $5 million – with defined thresholds and limits.
- Like First-Time Home Buyer Incentive, the market could benefit from a first-time investor program for new developers entering the market.
- Create a pre-approved builders list to expedite the process of guarantees.
- Consider how to deal with slide offs in covenant funds.

- Offer different financing solutions to suit the different motivations of developers, while considering their varying net-worth and expertise.
- Adapt programs like BMO's 'small business' category, which opens some space for $2-5 million developments without balance sheets and net-worth requirements.

Lending mechanisms in bigger markets

- High-rise development can be combined with affordable middle housing in bigger markets like Toronto and Vancouver.
- Multiple sites can be developed simultaneously. While such a solution would require more equity and effectively more risk, it could work for homeowners as land value can be counted towards equity, and leasing the land to developers makes the building less expensive.
- Current tax regulations need to catch up to the practice, and encourage upgrades to existing properties rather than new builds. Property tax credits or other tax incentives can be imposed at the municipal level for conversions and new builds (for example, no HST credit charged).

Ward level implementation

- Cultivate partnerships between nonprofit organizations and developers – take a zoomed-out view of collaborative relationships between nonprofit housing providers and developers that consider ward level distribution, over site specific. At the ward level, contribution of a nonprofit organization in the form of land and partial construction costs, makes it much more cost effective for developers to invest on nonprofit owned sites to offset market units within their own different development sites within the same ward.
- Design a new financing model that allows the development of two buildings on different sites in the same ward under one application of multi-lot financing. The model would require one to be market priced and the other to be affordable.

Uniformity

- The federal government should work with banks and lenders to encourage them to offer the options required by the new generation of SME developers.

SESSION 3: KEY TAKEAWAYS AND ACTIONS

The final hour was dedicated to individual reflections. Each participant shared takeaways and learnings from the sessions. The most common takeaways were the need for transparency about the risks associated with the full range of multiplex developments, and the need to design new financial products to suit their needs. The group agreed that a collaborative approach and continued conversation is needed to bring the actions to life.

Below is the consolidated list action items, and some next steps from the group.

Takeaways

- Middle housing needs middle financing. There is a gap in the market, as the options for small scale developers are extremely limited.
- Lots of developers that do not fit into traditional bank boxes are considered risky and not worthwhile engagements as they tend to fall between residential, commercial and investor profiles. Explore the lending appetites for owner-occupied developers and investor-developers.
- Each customer profile has a different level of associated risk that needs to be accurately assessed, managed, and communicated.
- Housing affordability and energy-efficient design solutions need more attention from a lending perspective.

Recommended actions

- Conduct a gap assessment to understand the associated risks in financing different types of customers: homeowner vs investor vs speculator
- Explore missing middle financing as a separate category with clearly defined guidelines, limits and thresholds.
- Work collaboratively to remove the stigma around investor-developers, and equip homeowners and small-scale developers with the right resources, knowledge, and tools to assess their options.
- Consider developing a first-time investor program for middle housing development.
- Follow up on engagement between participants to explore collaboration and referral partnerships.

OFF-SITE CONSTRUCTION (VOLUMETRIC MODULAR)

Facilitated by Jeanhy Shim, President and CEO, Crosswalk Communities; Advisory Board, Infrastructure Institute at the University of Toronto

HSC innovators

Vancity enhances access to capital for early-stage planning and pre-development costs for community housing projects through its Affordable Housing Accelerator Program. They are working on expanding the program across Canada in partnership with other credit unions.

1. Director of Social Finance, Irene Gannitsos represented Vancity Community Foundation

BuildingIN helps municipalities to navigate the challenges and barriers in increasing their housing supply with multi-unit low-rise infill housing. They get that done while helping municipalities create vibrant, complete communities with their volumetric modular designs.

2. Principal Architect, Rosaline Hill and 3. Director, CityShapes, Neil Saravanamuttoo represented BuildingIN

L'Unité de travail pour l'implantation de logement étudiant (UTILE) is a non-profit organization works to improve the living conditions of the student population by developing sustainable living environments, built to a high quality and adapted to their needs.

4. Director of Investment, Isabelle Therien represented UTILE

Participants

	Name	Organization	Title
5.	Kevin Corbett	Vancity Investment Bank	Senior Manager, Business Development, Commercial Real Estate
6.	Sam Drysdale	BMO	Director, Real Estate Finance
7.	Jacqueline Evans	Former NRB Modular Solutions	Modular Affordable Housing Consultant
8.	Apar Jain	CMHC	Advisor, Risk Management, Strategy & Products - Multi Unit Housing
9.	Mukhtar Latif	Crosswalk Communities and Pomegranate Housing Consultancy	Co-founder and Chief Executive Officer
10.	Amrish Manna	Peoples Group	Assistant Vice President, Commercial Real Estate
11.	Rob Stansfield	Meridian Credit Union	Vice President and, Head of Corporate and Structured Finance

SESSION 1: PROBLEM STATEMENT DEEP DIVE

Through a pre-workshop survey and a discussion during the first session of the forum, we gathered thoughts from the innovators and participants on the financing challenges they and/or their clients face in financing modular developments. Their responses and the participants' discussions are collated for both non-market and market housing.

Non-Market Housing

Deposit challenges with CMHC and traditional financiers: The participants discussed that in their experience, CMHC and traditional financiers do not accept deposits, which forces non-market housing developers (such as UTILE) to borrow from non-conventional lenders, which results in higher interest rates. Consequently, unit costs increase, making it difficult to scale and replicate affordable housing projects.

Cash flow in modular construction: Modular construction involves a compressed cash flow, with higher upfront payments required over a shorter period compared to conventional construction.

Example: UTILE is developing a pilot project to build 155 affordable units in a small town. This required a $3 million deposit for the whole project. They could not access CMHC financing products or conventional financing products to meet the deposit requirement. They overcame this hurdle by securing a land donation from the City, and the Province of Québec covered one third of the project cost (approx. $9.5 million). The remaining amount was funded by CSII (a syndicate of lenders with patient capital) in the form of a construction loan with a floating interest of 7-8%. Overall, the project requires $23 million in nine months. The ad hoc approach being employed for this project may not work for other projects, making replicability and scaling of non-market modular projects almost impossible.

Notes from participants' discussion

- **Advantages of modular:**
    - Lower risk for financiers: Participants discussed that shorter timeline of modular projects reduces financial risk, as market fluctuations are less likely to occur. For example, when materials are purchased upfront, the chance of price changes during the relatively brief manufacturing period of modular construction is minimized.
    - Improved market feasibility: Participants thought that market feasibility is more stable with modular construction due to its shorter project timeline – typically one year compared to three years for conventional construction – reducing the likelihood of market changes during the development process.
    - Easier access to construction loans: Based on their experience, participants mentioned that shorter timeline of modular projects simplifies access to construction loans, as lenders face reduced risks associated with market fluctuations and project delays.
- **Post construction:**
    - Participants agreed that operating costs are easy to maintain without a subsidy for non-market modular housing for students.

Market housing

Lender reluctance in modular construction: Participants find that lenders are hesitant to finance developers operating in the emerging modular construction market due to perceived risks. These stem from the involvement of relatively new market players and the absence of materials on-site for most of the project duration during manufacturing. As a result, financial products are lacking for small-scale infill modular projects, typically developed by builders working on $3-5 million projects with 8-10 units on older lots.

Misconceptions about modular construction: During the session participants mentioned that there seem to be some common misconceptions about modular construction, particularly regarding its permanence and the variety of modular types available. That make them less appealing to banks. This issue is further compounded by the acquisition of Canada's largest modular builder by the country's largest trailer manufacturer. The participants suggested that education and awareness are needed to correct these misconceptions.

Example: BuildingIN collaborates with municipalities on regulatory overlays and investment strategies to pave the way for volumetric modular construction, allowing builders to increase their annual unit output by 8 to 12 times through repeatable multi-unit designs. However, the BuildingIN noted that the expansion is not feasible without access to financing for modular construction.

Typically, builders or developers working with modular methods pay 25% upon contract signing, 25% upon material procurement, 25% when the modules are completed, and the final 25% upon delivery to the site. BuildingIN commented that the traditional construction financing relies on materials being present on-site and that's what financiers look for, making it nearly impossible to finance the first three payments for modular projects. This financing challenge affects both small developers who focus on 6– to 12-unit buildings, as well as larger developers, though the scale of the issue varies. The participants suggested that a certificate from CMHC could provide financiers with the assurance needed to offer loans under these conditions. BuildingIN also noted that even if all other barriers to modular housing are removed, the full potential for rapid housing delivery cannot be achieved without appropriate financial products and loan guarantees.

Notes from participants' discussion

- **Budget allocation in modular vs. conventional construction:**
  - Participants stated that the construction budget for modular projects typically represents 40-85% of the total project budget, compared to 25-30% in conventional construction – figures more familiar to traditional financiers.
- **Building familiar products:**
  - Small to large businesses are quick in responding and adapting to familiar products if available. For example, such businesses have frequently accessed Mortgage Loan Insurance (MLI) program for financing. Therefore, the participants expressed that building modular financing onto existing products would be beneficial.
- **Financing challenge in modular construction:**
  - Participants agreed that a key issue is the tendency to treat manufacturing financing the same as construction financing, ignoring the distinct parameters and requirements of each.

- **Solution through diverse financiers:**
    - One participant's suggestion involved engaging financiers with higher risk tolerance to accommodate the unique challenges of modular construction.
- **Where it worked:**
    - Participants indicated that further research of case studies and data is needed to inform decision making and financial product creation in Canada. There are some examples from the U.K. where the government stepped in and provided a guarantee for the first round of the nascent build-to-rent purchase. This provided comfort and trust in the lending market to finance such projects. Perhaps, similar experiences could be transferred to modular housing.
    - Modular construction has been in production for school campuses since 1979, so it is not a new concept. However, there is reduced risk in schools due to their high demand (manufacturers can build modules on spec keeping the production line running). If the same point of spec production can be achieved for housing, the deposit issue may be resolved, though a new financial challenge will arise as developers will have to buy the whole building at once as there will be no manufacturing lead time, and the modules will be bought off-shelf.
- **Why aren't banks and financiers filling this gap in the market?**
    - Participants find that the concept and market for modular housing may be too new to Schedule A banks, who perceive it as a risky and untested endeavour. For these banks to support modular construction, several adjustments, and more information are needed to fill this gap. Key concerns include the developer's experience and track record with modular projects, as well as the lack of security for off-site products, which remain off-site for much of the project duration.
    - Participants noted that financiers look at leverage, cashflow, and strength of guarantee amongst other items.
    - Participants also mentioned that if assets exist outside the construction site, there are insurance products that can ensure that the bank/financier is covered. However, not all insurers would qualify for this type of project.
    - Based on the participants experience, to determine pricing on such loans, banks will need to conduct some research through case studies, and big projects.
    - Through the participant discussion it was obvious that different financiers operate with varying levels of flexibility and objectives. For example, credit unions, while for-profit, have the discretion to set their profit margins, but in contrast, banks are for-profit institutions accountable to shareholders, which limits their flexibility.
    - Participants noted that having a reasonable value in the security of the land relative to the loan size would be helpful for lenders.
    - Participants expressed that the size, scale, and volume of business need to be convincing for the banks (i.e., five affordable units may not be sufficiently attractive).

*Lenders are **hesitant to finance developers operating in the emerging modular construction** market due to perceived risks.*

SESSION 2: SOLUTIONS BRAINSTORM

After determining the problem statements and diving deep into the main issues facing modular financing, the participants discussed and brainstormed potential solutions for both market and non-market modular construction financing.

Non-market housing

Deposits for affordable housing: Participants suggested that CMHC could pay the deposits for affordable housing to enable providers to access finance and to reduce the upfront costs.

Establish a pre-approved list of modular manufacturers and developers: Participants agreed that establishing a list based on criteria such as experience, credit history, and portfolio would help eliminate or relax deposit requirements, facilitating access to smoother financing options. This list, if approved by CMHC, could pave the way for non-market housing developers to secure capital from conventional lenders, ultimately lowering interest rates.

The participants expressed that the framework for preapproval should be relatively simple to implement and would provide lenders with greater confidence, helping to reduce their perceived risk. However, while the list would offer assurances, lenders would still need to conduct their own independent underwriting.

Furthermore, participants suggested that partnering with institutions like the Modular Building Institute could play a part in developing that list, for example by establishing guidelines and parameters, but not as adjudicators (to avoid conflict of interest). They also suggested that the University of New Brunswick's research hub for modular construction might be a good candidate to help in the development of this list and framework.

It would be essential to specify the type of modular construction included in the list. Participants suggested starting with volumetric modular construction, as it is more prevalent, thoroughly tested, and particularly affected by deposit challenges compared to other modular types.

Find alternative partners for a quick injection of money: Based on their experience, some participants indicated that finding investors with ESG policies or other common targets with non-market housing providers could provide access to capital.

Create CMHC developer programs: Participants emphasized the need to create programs to facilitate financing for developers that work in modular construction.

Market housing

(Note: the following suggested solutions could apply to both market and non-market housing. However, the suggested pilot would be volumetric and market, to reduce variables)

Creating a government loan guarantee program for modular construction: Creating a program for modular construction would allow financial institutions to participate under strictly defined criteria, distributing risks among lenders, developers, and the government. Financiers participating in the Forum expressed that with a government-backed guarantee in place, they would provide capital without hesitation.

The suggested guarantee could be short-term, expiring once construction financing becomes viable. It would function like seed capital, providing early-stage support without requiring upfront investment. This risk-sharing mechanism can enable projects that might otherwise stall, giving all parties – lenders, developers, and the government – a shared stake in success. The idea of having a guarantee program to kick start the market is not new and has been implemented by the government in other programs, and in the U.K. Once the lenders become familiar with the product and understand the risks, the program can be phased out.

Participants think that lenders must play an active role in initiating insurance products by identifying their concerns and proposing the types of coverage they need to feel secure in lending. They also think that CMHC could then evaluate these proposals and design appropriate insurance solutions.

Pilot programs could also support this guarantee initiative, similar to the pilots conducted under the Mortgage Loan Insurance (MLI) program. Rather than developing new financial products, the participants proposed that the program could modify existing loan products, which would be simpler, faster, and less complex to implement.

A notable example of risk-sharing exists in British Columbia, where a program designed to promote affordable homeownership splits financing between private lenders and the government. In this model, conventional lenders finance 60% of the project, while the provincial government underwrites the remaining 40%.

Create a pilot program with selected lenders to work with CMHC to come up with a product: Participants expressed that a pilot program with selected lenders, in collaboration with CMHC, could be an effective way to develop financial products for modular construction. This initiative would allow for experimentation and innovation while addressing the unique challenges of financing modular projects.

Vancity Investment Bank expressed their willingness to experiment with financial products and participate in pilot programs, making them an ideal partner to explore solutions that could shape future modular financing frameworks.

The participants further suggested that the pilot program could also strategically partner with innovative municipalities (such as Hamilton) who could provide the guarantee for the pilot. These municipalities could further support the endeavor by eliminating zoning restrictions and other red tape. Selecting a strategic municipal partner that can act quickly and address both financial and non-financial barriers is essential to the pilot's success.

Improve insurance products: The participants also shared ideas on insurance-backed Mortgage Loan Insurance Select (MLI Select) product targeting the concerned segment, and insurance until delivery that would cover the lender.

SESSION 3: KEY TAKEAWAYS AND ACTIONS

The participants agreed that leveraging private capital is essential for implementing the National Housing Strategy. This requires political will, combined with financiers' will and proactivity in creating financial products. All participants in the forum – government, not-for-profit, and for-profit organizations – showed willingness to contribute to finding and implementing solutions in their capacity. Following is a list of the discussed next steps and actions in the path towards workable financial solutions for both market and non-market modular housing construction.

Immediate recommended actions

General:

- Research, data, and knowledge mobilization:
  - Create an information hub to collect research, data, and case studies on modular construction, both nationally and internationally, with a focus on financing
  - Reach out to the Canadian Homebuilders Association to check their available resources that could be added to the hub, including their recent or ongoing research about modular construction financing
  - Explain and explore the potential role of different government levels in enabling modular construction financing
- Create a summary document:
  - Compile a report with clear action items from this forum and reconvene to strategize stakeholder engagement and implementation of the proposed actions

Non-market housing:

- Engage more lenders in affordable housing financing by sharing this report and raising awareness about potential collaborations
- Create a capital stack spreadsheet showing contributions from government, insurers, foundations, and lenders (e.g., municipal land donations) to map out risks, benefits, time requirements, and potential financing partners
- Initiate work on the pre-approval list of modular manufacturers and developers, focusing on experience and credit history, by engaging CMHC and other partners.

Market housing:

- Engage innovative municipalities, such as City of Hamilton, to participate in the pilot to explore their role in financing modular projects, including offering guarantees and easing zoning restrictions
- Vancity will propose a modular housing pilot as their test-and-learn at their next strategy session
- Design a scalable pilot project that tests financing solutions for modular construction with selected lenders and municipal partners
- Draft a proposal and engage the relevant housing stakeholders and decision makers by sharing the findings of this forum with the backing of participants
- Build momentum and pressure by involving the media and publicizing the findings

Short-term recommended actions

General:

- Keep updating and adding content to the information hub

Non-market housing:

- Create a framework for a list of pre-approved builders and developers

Market housing:

- Start working on a scalable pilot project for financing volumetric modular market housing projects

Long-term recommended actions

General:

- Plan policy changes and long-term initiatives with CMHC that align with modular financing goals
- Study the outcomes of the pilot project and design a scalable financial product tailored for non-market modular housing
- Use the insights from the pilot project to develop a financing product that supports the growth of modular construction in the market housing sector

CONCLUSION

The forum showed that ADUs, multiplexes, and off-site modular construction financial products are at different levels of market maturity. ADUs seem to be more mature and moving rapidly towards dedicated and customized financial solutions that enable their creation. On the other hand, multiplexes and off-site modular housing products seem to be in early stages or even non-existent, with clear gaps in the financing market.

The proposed solutions and subsequent next steps are good starting points to stir a change towards removing financial barriers that inhibit housing unit creation. Some common recommendation themes included education, raising awareness, creating pilot products, collaboration, and governmental programs. While this forum initiated the discussions, further actions and wider stakeholder involvement will be needed to enact tangible change on the ground.

NOTES

1. Instances where the homeowner builds new housing for additional income.

2. Instances where the developments' purpose is to house family members: in-laws, aging parents, adult children, family guests etc.

3. Instances when the owner is not occupying any of the units within the multiplex and is developing for additional income.

4. The Four Cs of Credit are Character, Capacity, Capital and Collateral.

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